

Proposition 72**Referendum Petition to Overturn Amendments to Health Care Coverage Requirements.****BACKGROUND****Health Coverage in California**

A majority of Californians under age 65 receive health insurance through their employer or the employer of a family member. Most Californians age 65 and over are covered by the federal Medicare Program. Others purchase health insurance for themselves. Many individuals receiving coverage share in the cost of the premiums paid for their health insurance.

Many low-income persons obtain health care services through the Medi-Cal Program, the Healthy Families Program, or other public programs operated by the state and county governments. Medi-Cal is administered by the state Department of Health Services (DHS), while the Healthy Families Program is administered by the state Managed Risk Medical Insurance Board (MRMIB). However, based upon a 2001 survey, an estimated 6.3 million nonelderly Californians lacked health coverage at some point during the year. These individuals are likely to receive medical assistance from county indigent health care programs or through the charitable activities of health care providers or pay for it themselves. Surveys indicate that of the nonelderly uninsured individuals, more than four out of five are either employed or are family members of someone who is working.

Some of the medical costs incurred by uninsured persons are indirectly shifted by health care providers to others who have health coverage, in effect adding to the cost of their health insurance. There are also indications that the number of employees who are uninsured may be adding to the costs of workers' compensation insurance, which includes medical coverage for on-the-job injuries.

Recent Legislation

In 2003, the Legislature approved and the Governor signed Senate Bill 2 (Chapter 673) to expand health insurance coverage beginning in 2006 for employees of certain employers and, in some cases, their dependents. The law also established a program to assist lower-income employees with paying their share of health care premiums.

The new law would have gone into effect January 1, 2004. However, Proposition 72, a referendum on this new law, subsequently qualified for the statewide ballot. As a result, SB 2 was put "on hold" and will take effect only if Proposition 72 is approved by the voters at the November 2004 election.

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Proposal

If approved, this proposition would allow the provisions of SB 2 to go into effect. Health care researchers have estimated that the provisions of SB 2 could eventually result in more than 1 million uninsured employees and dependents receiving health coverage. The major provisions of SB 2 are described below.

"Pay or Play" Requirement for Employers

Senate Bill 2 enacts a "pay or play" system of health coverage for certain employers. Under the system, specified California employers would be required to pay a fee to the state to provide health insurance (in other words, "pay") for their employees and in some cases, for their dependents. Alternatively, the employer could choose to arrange directly with health insurance providers for coverage (in other words, "play") for these individuals.

Both "pay" and "play" employers are required to pay a fee to the state to support a state health insurance purchasing program. Employers choosing to arrange their own health coverage (in some cases by continuing or modifying the coverage now provided to their employees) would receive a credit that would fully offset their fee. In order for an employer to qualify for a fee offset, the employer would have to provide specified types of coverage. Employers would be responsible for at least 80 percent of the cost of the fee, with the balance borne by their employees. The fee would be collected from employers and the fee requirements enforced by the Employment Development Department (EDD).

Senate Bill 2 would generally apply to both private and public employers, including state government, counties, cities, special districts, and school districts.

Federal law, known as the Employee Retirement Income Security Act, has been interpreted by the courts to generally prohibit states from requiring certain employers to provide health insurance coverage to their employees. As a result, it is possible that the "pay or play" provisions of SB 2 could be challenged in court. Our analysis assumes that the "pay or play" provisions would go into effect.

Who Would Provide and Receive Coverage?

Figure 1 summarizes which employers are affected by the "pay or play" requirements, when they would be subject to the requirements of SB 2, and who would receive health coverage. These requirements depend upon the number of employees an employer has in California. Senate Bill 2 also provides that employers with 20 to 49 employees would be subject to the "pay or play" provisions only if state law were changed to establish a tax credit for those employers equal to 20 percent of their state fee for health coverage. To date, no such tax credit legislation has been enacted, and these employers are currently exempt from the provisions of SB 2. Employers with 19 or fewer employees within California would not be subject to its requirements.

**SUBJECT TO COURT
ORDERED CHANGES**

Figure 1**Which Employers Are Affected by This Measure?**

Employers Who Employ...	... Must Provide Health Coverage to...	Starting
200 or more employees in the state	Employees and dependents	1/1/06
50 to 199 employees in the state	Employees only	1/1/07
20 to 49 employees in the state	Employees only, if a specified tax credit is enacted	Undetermined
19 or fewer employees in the state	No requirement	Not applicable

Any employee who worked more than 100 hours per month for the same employer for three months would qualify for health coverage. Senate Bill 2 defines the list of dependents who could be eligible for coverage to be spouses, minor children, older children who are dependent upon the employee for support, and domestic partners.

Senate Bill 2 imposes penalties on any employer who reduces an employee's hours of work or takes other steps to avoid having to comply with its "pay or play" requirements.

Contributions by Employees

Employees would generally be required to make a contribution of up to 20 percent of the amount of the fee charged by the state to their employer. Contributions paid by employees would be collected by their employer and transferred to the state.

Low-income employees would have their contributions capped at 5 percent of their wages. Senate Bill 2 defines a low-income employee as an individual who earned wages of less than 200 percent of the federal poverty guidelines—currently about \$19,000 a year in the case of an individual, and about \$31,000 a year in the case of an employee and his or her family.

In addition to these contributions, employees could also be charged part of the additional costs for their coverage in the form of deductibles, copayments, or coinsurance payments in amounts determined by the state. These charges would have to be set at a level that took into account whether the persons would be deterred from obtaining appropriate and timely health care.

State Health Purchasing Program

Senate Bill 2 creates the State Health Purchasing Program to purchase health care coverage for eligible California employees (and their dependents) of employers who opt to pay a fee instead of arranging for health insurance. The purchasing program would be administered by MRMIB. The MRMIB would negotiate contracts with health insurers, primarily private health plans, who agreed to provide health care coverage. The coverage would have to meet existing state standards for health insurance, such as

**SUBJECT TO COURT
ORDERED CHANGES**

the inclusion of hospital and primary care, and would also include coverage for prescription drugs. The cost of health coverage purchased under the program, as well as MRMIB's and EDD's administrative costs for the implementation of the program, would be supported with the funds collected from employers and employees under SB 2.

State Premium Assistance

Senate Bill 2 establishes a program to pay the premiums for health coverage provided through the workplace for low-income employees who are eligible for Medi-Cal or the Healthy Families Program. This provision applies to eligible employees for all California employers, and not just those employees of employers affected by the "pay or play" requirements of SB 2. So, for example, eligible employees of employers that provide health coverage and that have fewer than 20 employees would qualify for premium assistance.

Under the premium assistance program, the state and employers would notify employees of the availability of premium assistance and employees may voluntarily provide information to the state that would indicate if they and their families were eligible for coverage under Medi-Cal or the Healthy Families Program. If these persons were subsequently enrolled in either public program, the state could require them to also enroll in any coverage available from their employer, if that were determined by the state to be cost-effective. The state would reimburse these employees for any premiums they paid for the coverage provided by their employer. However, these employees would remain subject to paying any premiums and copayments required under Medi-Cal or the Healthy Families Program.

Employees and their families receiving premium assistance would also receive what is known as "wraparound" coverage from the state. In this case, this means that the state would provide and pay for any additional medical services for an employee or their family that were included in either the Medi-Cal or Healthy Families benefit package (such as dental coverage), but that were not included in the health coverage provided by the employer.

The implementation of the state premium assistance provisions would be the responsibility of MRMIB and DHS, and would be subject to approval by the federal government.

Health Insurance Marketing Provisions

Senate Bill 2 expands to medium-sized employers a series of provisions now in state law that are intended to make it easier and more affordable for small employer groups to purchase health coverage. For example, if a health plan or insurer offered and sold an insurance product to one medium-sized employer, they would be required to offer and sell the same product to other employers of similar size. Senate Bill 2 provides that,

**SUBJECT TO COURT
ORDERED CHANGES**

should its "pay or play" requirements be invalidated in court, these provisions affecting health coverage purchases by medium-sized employers would also become inoperative.

General Fund Loan

Senate Bill 2 authorizes loans from the state General Fund, subject to appropriation in the annual budget act, for costs incurred by MRMIB and EDD for the establishment and administration of the State Health Purchasing Fund. The loans are to be repaid with interest within five years after the state begins the collection of fees from employers.

Fiscal Effects

The health coverage requirements of SB 2 would have a number of significant fiscal effects on state and local governments, including counties, cities, special districts, and school districts. In addition, they could have significant effects on individuals and businesses. These effects are complex, uncertain, and difficult to predict over time. Among the factors that could cause savings and costs to vary significantly are:

- How some provisions of SB 2 were eventually implemented by state and local officials and interpreted by the courts.
- The proportion of employers who chose to participate in the State Health Purchasing Program.
- How the health insurance marketplace responded to the new law in the products and prices it offered to public and private purchasers of care.

Given these uncertainties, we believe that the net savings or costs to the state and local governments are unknown. Our estimates assume that SB 2 affects employers with 50 or more employees. The more significant identifiable savings and costs to state and local governments that could result from this SB 2 are summarized below.

Purchasing Program Revenues and Expenditures

The "pay or play" requirements of SB 2 would generate significant revenues to the state from fees paid by employers that chose to "pay" for health coverage rather than to "play" by directly arranging their own health coverage. Also, the state would receive additional revenues from contributions for coverage paid by the employees of the firms choosing to "pay."

The state revenues received from these employers and employees would, in turn, be used to fully offset the costs of the State Health Purchasing Program. The most significant program costs would be for the purchase of health insurance coverage, primarily from private insurers, for employees of these employers (and, in the case of some employers, the dependents of these employees). These state revenues would also be used to fully offset administrative and other costs related to the State Health Purchasing Program.

**SUBJECT TO COURT
ORDERED CHANGES**

The proportion of employers who would choose to "pay" the fee to the state, thereby obtaining health coverage from the State Health Purchasing Program, rather than to "play" by arranging health coverage on their own, is a major unknown factor. The choices ultimately made by employers on whether to "pay or play" would have a significant impact on the amount of fee revenue paid to the state as well as the size of the State Health Purchasing Program. We estimate that the amount of fees collected from employers and employees and spent for the purchasing program could range from the tens of millions of dollars to the hundreds of millions of dollars annually, depending on the participation level of employers. This estimate assumes that the state collects the fee only from firms that choose to "pay" and not from firms that "play" by arranging health coverage on their own and therefore receive a credit that fully offsets their fee.

Effect on Other Publicly Funded Health Programs

State. The net effect of SB 2 on state-funded health programs is uncertain. Some provisions are likely to result in state savings while other provisions are likely to result in costs, as discussed below.

On the one hand, the "pay or play" requirement for employers to either pay a fee to the state or provide health coverage would generally have the effect of reducing state costs for Medi-Cal and Healthy Families benefits. This is because costs for these state-supported health coverage programs would likely decrease as additional employees and dependents received coverage from the State Health Purchasing Program or through coverage arranged by employers.

On the other hand, the premium assistance and wraparound coverage components of SB 2 would generally have the effect of increasing state costs for Medi-Cal and Healthy Families benefits. These provisions would result in the enrollment of additional employees and dependents in the two programs, additional state expenditures to reimburse employees for the premiums they paid for employer-based coverage, and additional state expenditures for wraparound coverage.

Taking all of these provisions and their fiscal effects into account, we estimate that the fiscal impact on Medi-Cal benefits would eventually be a net savings to the state amounting to tens of millions of dollars annually. However, we estimate that SB 2 would result in a net cost to the state for Healthy Families Program benefits of roughly the same magnitude. Given the uncertainties associated with SB 2, it is not clear at this time whether it would ultimately result in a net cost or savings to the state for state-supported health benefits.

Local. County costs for providing health care for indigents are likely to decrease significantly as more employees and dependents receive health coverage that is paid for by employers, Medi-Cal, and the Healthy Families Program. We estimate that the implementation of SB 2 would eventually result in savings to county governments on a statewide basis, potentially in the low hundreds of millions of dollars annually.

SUBJECT TO COURT
ORDERED CHANGES

State Administrative Costs

Senate Bill 2 specifies that part of the fees collected from employers would be used by MRMIB and EDD to offset their costs for administering the new State Health Purchasing Program. However, under the terms of SB 2, administrative costs incurred by DHS and MRMIB for the premium assistance program are not included among those that would be offset from fee revenue, and thus would probably be supported from the state General Fund and federal funds. We estimate that MRMIB, EDD, and DHS would incur significant administrative costs, probably amounting collectively in the low tens of millions of dollars annually, to implement SB 2.

Costs to Public Employers

The "pay or play" requirements of SB 2 generally apply to public employers, including the state, counties, cities, special districts, and school districts. Although full-time employees of public agencies in California usually have health coverage, some seasonal, temporary, and part-time employees and their dependents currently lack health coverage. We estimate that the additional cost to the state and local agencies to comply with SB 2 could potentially amount to the low hundreds of millions of dollars annually beginning in 2006-07.

These additional costs could be partially offset by savings to public agencies in certain circumstances. For example, some spouses of public agency employees would receive coverage from their own employers as a result of SB 2. Because these spouses would no longer receive coverage as dependents of employees of those public agencies, such agencies could realize some savings on their health coverage costs. The amount of the offsetting savings from this and other factors is unknown.

Effects on State Revenues

Senate Bill 2 would impact state revenues in two major ways.

First, some businesses would face increased operating costs to pay for employees' health insurance. To the extent that businesses absorb these costs, their taxable income would be less and, thus, income tax revenues would decline. Many employers would act to avoid absorbing these costs, however, such as by "passing them along" to consumers through higher product prices or to employees by cutting back on hours or wages. These steps could reduce overall economic activity, causing declines in personal income taxes and sales taxes. Revenue losses also would occur if California lost economic activity to other states.

Partially offsetting the above factors would be potential revenue gains due to any reduction in the health premiums that otherwise would have been paid by certain employers, as well as expanded economic activity in the health care sector. Current premiums paid by employers for health insurance and workers' compensation insurance may reflect some "cost-shifting" to cover health care costs of the uninsured. To the extent that SB 2 reduces the number of uninsured persons, it could reduce cost-

SUBJECT TO COURT
ORDERED CHANGES

shifting and could lower premiums paid by employers, thus increasing taxable income. In addition, employers' costs for complying with SB 2 may be reduced if the State Health Purchasing Program negotiates lower insurance rates, or the health care marketplace itself responds to SB 2 with reduced rates. Finally, the significant expansion of health coverage could increase state tax revenues paid by health plans and insurers.

Taking these and other factors into consideration, SB 2 would likely result in a net reduction in state tax revenues, potentially in the low hundreds of millions of dollars, with the actual magnitude depending on the behavioral responses of employers and the health care marketplace.

**SUBJECT TO COURT
ORDERED CHANGES**

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